In the Supreme Court of the United States

OCTOBER TERM, 1965

No. 1015

R. C. OWEN COMPANY, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

MEMORANDUM FOR THE RESPONDENT IN OPPOSITION

This case presents the essentially factual question whether, as both lower courts held, certain subordinated debentures issued by petitioner, a family-held corporation, constituted evidence of equity investment rather than indebtedness.

Petitioner was organized to acquire and operate the assets of a family partnership engaged in the manufacture of hardwood flooring and allied products. It issued 20,000 shares of $1 par value common stock and $340,000 of twenty-year 3½ per cent subordinated debentures to the former partners (a father and his two sons). (Pet. A9–A10.) The debentures provided in pertinent part (1) that all or any of their terms "as they affect the holders thereof" could be

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amended by a vote of 75 per cent (in principal amount) of the holders thereof, (2) that they were subordinated to "any and all indebtedness incurred by R. C. Owen Company, to banks or to others in the ordinary course of business," and (3) that action by 75 per cent of the holders thereof was necessary to accelerate maturity on default (Pet. A11). In each of the taxable years here in question (1954, 1955 and 1956) petitioner paid $8,400 "interest" on its debentures and claimed a deduction therefor. The Commissioner disallowed the claimed deduction on the ground that the payments did not constitute "interest" within the meaning of 1954 Code § 163 (Pet. A14). The Tax Court concluded that the Commissioner's determination was correct (Pet. A17), and the court of appeals affirmed (Pet. A1, A8).

This Court has ruled that whether a purported debt instrument is in reality an equity investment is essentially a question of fact, and that "There is no one characteristic, not even exclusion from management, which can be said to be decisive in the determination of whether the obligations are risk investments in the corporations or debts." *John Kelley Co.* v. *Commissioner,* 326 U.S. 521, 526–527, 530. The weight to be given to the various indicia is for the fact finder. The form of the transaction is not determinative of the question, and the taxpayer has the burden of proving by a preponderance of the evidence that the instruments were not representative of risk investments. *John Kelley Co.* v. *Commissioner, supra; Jewell Ridge Coal Corp.* v. *Commis-*

sioner, 318 F. 2d 695, 698 (C.A. 4); *Charter Wire, Inc.* v. *United States,* 309 F. 2d 878, 880 (C.A. 7); *Gilbert* v. *Commissioner,* 262 F. 2d 512, 513–514 (C.A. 2), certiorari denied, 359 U.S. 1002; *Gooding Amusement Co.* v. *Commissioner,* 236 F. 2d 159, 166 (C.A. 6), certiorari denied, 352 U.S. 1031.[1]

The evidence fully warrants the conclusions of both lower courts. The record indicates that the holders of 75 per cent of the debentures could amend the provisions thereof, *e.g.,* the maturity date and interest rate, and thus, "in substance," there was no definite maturity date or fixed interest rate; that the debentures were subordinated to any indebtedness incurred by the petitioner in the ordinary course of business; that only upon notice by the holders of 75 per cent of the debentures could the bonds be declared due and payable upon default; that the members of the Owen family originally held petitioner's debentures and stock in exactly the same proportions; and that the debentures were not issued in exchange for cash.

Petitioner's claim (Pet. 8–9) that the decision below conflicts with *Commissioner* v. *O.P.P. Holding Corp.,* 76 F. 2d 11 (C.A. 2), is without foundation.

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[1] Petitioner contends (Pet. 6–7) that the court of appeals erred in using the "clearly erroneous" standard to review the Tax Court's finding that the debentures constituted equity. However, the case law clearly establishes that this doctrine is applicable to a determination of the debt-equity status of particular instruments. See *Foresun, Inc.* v. *Commissioner,* 348 F. 2d 1006, 1008 (C.A. 6); *Jewell Ridge Coal Corp.* v. *Commissioner, supra,* at 696; *Brake & Electric Sales Corp.* v. *United States,* 287 F. 2d 426, 428 (C.A. 1).

Neither the provisions of the debentures in issue in *O.P.P. Holding Corp.* nor the circumstances surrounding their issuance were even remotely similar to the instant case. The decision below is in complete accord with decision of the Court of Claims in *R. C. Owen Co.* v. *United States,* 180 F. Supp. 369, certiorari denied, 363 U.S. 819 (see also *R. C. Owen Co.* v. *Butler,* 387 S.W. 2d 830) reviewing debentures issued by a sister corporation of petitioner and containing provisions substantially identical to those here in issue. Finally, the Trust Indenture Act of 1939, c. 411, 53 Stat. 1149, § 316 (15 U.S.C. 77 ppp), referred to by petitioner (Pet. 7), is not relevant to the instant case, since that statute deals with publicly offered evidences of indebtedness.

The petition for a writ of certiorari should be denied.

Respectfully submitted,

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